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In the Supreme Court
OF THE
United States

OCTOBER TERM 1945

No. 834

LA SOCIETE FRANCAISE DE BIENFAISANCE MUTUELLE (a corporation),
Petitioner,

vs.

UNITED STATES OF AMERICA.

PETITION FOR WRIT OF CERTIORARI
to the Circuit Court of Appeals for the Ninth Circuit
and
BRIEF IN SUPPORT.

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No.

LA SOCIETE FRANCAISE DE BIENFAISANCE MUTUELLE (a corporation),
Petitioner,

vs.

UNITED STATES OF AMERICA.

PETITION FOR WRIT OF CERTIORARI.

To the Honorable Harlan Fiske Stone, Chief Justice of the United States, and to the Honorable Associate Justices of the Supreme Court of the United States:

Your petitioner, La Societe Francaise de Bienfaisance Mutuelle, of San Francisco, California, respectfully prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Ninth Circuit entered December 3, 1945, (rehearing denied January 2, 1946),

in an action numbered and entitled on its docket, No. 11,029, *United States of America,* Appellant, vs. *La Societe Francaise de Bienfaisance Mutuelle,* a corporation, Appellee, reversing the judgment of the United States District Court for the Northern District of California, Southern Division, in favor of petitioner for the sum of $35,269.85, this being the amount of taxes, interest and penalties which it had paid, under the Social Security Act,[1] for the years 1936-1942, inclusive.

SUMMARY STATEMENT OF THE MATTER INVOLVED.

In 1937 the Commissioner of Internal Revenue held that petitioner, as a charitable corporation, was exempt (R. 45). In 1939, this ruling was reversed (R. 46). The reason for the change does not appear, but the Commissioner's letter states that "it appears you are not operated for profit" (R. 45-46). Petitioner, in addition to *its own* tax ($21,719.29), has paid $13,550.56 for *employees'* taxes which had accrued before this reversal, interest and heavy penalties (R. 15).

Petitioner contends that, as a nonprofit corporation whose membership is unlimited and whose only purpose is the operation of its hospital and the treatment of the sick (R. 38), it is a "charitable" corporation within the meaning of Sections 811(b)(8) of Title VIII, and of Section 907(c)(7) of Title IX, of the

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[1] 49 Stat. c. 531, p. 620.

Social Security Act,[2] each of which provides that "the term 'employment' does not include";

> "Service performed in the employ of a corporation, community chest, fund or foundation organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual."

Petitioner was founded in San Francisco in 1851 (R. 38). In 1856, it was incorporated by the filing of a certificate which, under the statute,[3] stated only that the members had elected certain named trustees and had determined that they and their successors should forever be known by petitioner's present name (Plff. Ex. No. 11, R. 168). Prior to 1941 (R. 90, 119), a by-law provided:

> "The Society is founded on the basis of mutuality for the treatment of sick members; neither political not religious questions can ever be considered in its midst."

Since petitioner's activities are by no means confined to "the treatment of sick members", this is evidently an *admonition* as to political or sectarian activities.

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[2]Now I.R.C. Sections 1426(b)(8) and 1607(c)(8).

[3]Chapter VIII of Corporation Act of 1850, "Relating to Religious and other Associations or Societies" (Stats. 1850, at p. 373).

Petitioner has no capital stock, and no interest, dividends or other pecuniary distributions have ever been paid to anyone (R. 38-39). Its directors, who manage its affairs, serve without compensation (R. 39). Any net earnings have always been devoted to the improvement of its plant and the betterment of its services (R. 39, 156).

During the period involved, membership has averaged about 9,800 (R. 43). Their number is unlimited, and it has always admitted new members, (R. 43, 163, 181). Admission to membership is limited to persons (wholly or partly) of French birth or origin, or speaking French, (this is applied with liberality), or the spouse or child of a qualified member (R. 117, 142).

Petitioner owns and operates in San Francisco a large modern hospital[4] equipped to treat every kind of illness (R. 40), with a capacity of two hundred twenty-five beds and a nursery for children. The hospital site and buildings represent its principal asset, in addition to which it has moderate reserves. The services of the hospital are not restricted to members, but it is open to the public without distinction as to race, creed or color (R. 40). It provides for the training of interns (R. 41), and at large expense maintains a nurses' training school (R. 41).

Monthly dues are $1.75, but children, one of whose parents is a member, pay one dollar (R. 43). Life

[4]Approved by American Medical Association and by American College of Surgeons as a Class "A" Hospital (R. 40).

members, who have prepaid in full, otherwise have the same rights and privileges.

Continued payment of dues is not, however, a condition to relief. In the case of indigent member-widows and of other needy members, such dues are paid from petitioner's *relief fund* set up, in 1905, for that purpose (R. 78-79). A member under seventeen years, if orphaned or abandoned by his parents, pays no dues, nor do members in the armed forces of the United States, nor do student nurses, when members (R. 43). It gives other forms of purely gratuitous relief (R. 42).

The benefits are remarkable in their extent, variety and duration (R. 44). To its members and to the public, petitioner gives other very substantial services, either gratuitously or at cost (R. 42).

During its existence, petitioner has received donations and bequests aggregating $362,822.63 (R. 39) which, with the income therefrom, has amounted to over $500,000, or more than half its assets (R. 85). Without them, it could not have acquired its present plant nor give the service it renders (R. 39). In times of need, it has received other forms of public assistance (R. 171-173).

In its eight fiscal years ending February 29, 1944, petitioner has had *no* net income. Disbursements exceeded receipts by $35,283.96. Surplus decreased $65,682.95, (R. 80, 156). Improvements and maintenance amounted to $125,000. In the seven years ending February 28, 1943, disbursements had exceeded

receipts by $105,134.08. In the eight-year period, somewhat less than half of petitioner's total receipts was from non-member patients. *The latter pay only the prevailing rates in San Francisco* (R. 143-144). Normally, member patients greatly out-number others, (Plff. Ex. No. 10, R. 168). In addition, in those eight years, members' calls and consultations in the out-patient department averaged 33,734 per annum (R. 75). In June, 1944, there were about eight hundred members in the armed forces (R. 167).

Moreover, the 1944 excess in receipts was temporary, because appellee's hospital, like others, has been operated to capacity (R. 158). When conditions are again normal, receipts will decline, but wages and other expenses will probably continue permanently higher. The 1944 "profit" will have been illusory.

OPINION BELOW.

The opinion of the Circuit Court of Appeals is reported in 151 Fed. (2d) ....., and appears in the record (R. 196). The opinion of the District Court (R. 29-37) is reported in 57 Fed. Supp. 201.

Briefly, the reasoning of the Circuit Court is that, to be exempt, petitioner "must be devoted to charitable purposes exclusively"; that treatment of non-member patients is a substantial "non-charitable purpose" and constitutes a "business venture" and an independent "field"; that, by reason of these expanded operations and the enlarged income therefrom, its

plant and facilities were improved, and that this was a valuable service "which inured to the benefit of members."

STATEMENT OF BASIS OF JURISDICTION.

The judgment of the Circuit Court of Appeals was entered December 3, 1945 (R. 195). Rehearing was denied January 2, 1946 (R. 206).

The three months' period for filing this petition begins to run from January 2, 1946. Jurisdiction of this court is invoked under Act of February 13, 1925, Ch. 229, Sec. 1, 43 Stat. 938, as amended, Judicial Code, Sec. 240(a), U. S. C. Title 28, Sec. 347(a).

Jurisdiction was conferred on the District Court by Section 24, Twentieth, of the Judicial Code, as amended. Its judgment was entered October 13, 1944, (R. 56-58). Within three months, and on January 9, 1945, notice of appeal was filed (R. 58) pursuant to Section 128(a) of the Judicial Code, as amended.

QUESTIONS PRESENTED.

Whether the Circuit Court of Appeals erred:

1. In refusing to give effect to the intention and purpose of Congress to exempt "hospitals not operated for profit";

2. In holding that the treatment of non-member patients is one of the "purposes" for which petitioner was organized and is operated;

3. In holding that the clause, "no part of the net earnings of which inure to the benefit of any private shareholder or individual", has reference to the *source,* instead of the *use,* of petitioner's earnings, and that *receipt* of payments by such non-member patients, rather than the *use* thereof, determines its charitable character within the meaning of the Act;

4. In holding that petitioner is not entitled to recover the employees' tax ($6,195.77) which accrued before the 1939 reversal in ruling, which it paid from its own funds and for which it was not reimbursed; penalties ($4,996.05), and interest ($2,358.74).

REASONS RELIED UPON FOR ALLOWANCE OF WRIT.

1. The legislative history of the Act makes it unmistakably clear that Congress intended to exempt "hospitals not operated for profit". Hence, on November 2, 1943, the Attorney General, in a written opinion to the President, held that such legislative history "clearly shows that the language of the exemption in the statute was adopted by the Congress with knowledge that it had been construed to exclude nonprofit hospitals", and that Congress intended that "the exemption of the Social Security Act would receive the same construction," (40 Op. A. G. No. 72, infra, p. 19).

The opinion of the Circuit Court ignores this basic aid to construction, disregards and thwarts the inten-

tion of Congress, and substitutes for the determination of Congress its own view as to the desirability of exempting non-profit hospitals such as that of petitioner.

2. The decision of the Circuit Court of Appeals ignores, but is directly contrary to, *Trinidad v. Sagrada Orden,* 263 U. S. 578, 44 S. Ct. 204, 68 L. Ed. 458, which holds that exemption is not lost by using income, from whatever source, to further the purposes which are made the basis for the exemption.

The decision entirely misconceives, and so is directly contrary to, *Better Business Bureau v. United States,* 326 U. S. ....., 90 L. Ed. 76, 66 S. Ct. 112, where the corporation's "purposes" are held to be controlling.

3. The decision directly conflicts with

Commissioner v. Kensico Cemetery, 2d Circ., 96 Fed. (2d) 594;

Koon Kreek Klub v. Thomas, 5th Circ., 108 Fed. (2d) 616;

United States v. Proprietors of Social Law Library, 1st Circ., 102 Fed. (2d) 481;

Roche's Beach, Inc. v. Commissioner, 2d Circ., 96 Fed. (2d) 776;

Santee Club v. White, 5th Circ., 87 Fed. (2d) 5;

Scofield v. Corpus Christi Golf & Country Club, 5th Circ., 127 Fed. 452;

District of Columbia v. Mt. Vernon Seminary, 100 Fed. (2d) 116;

all of which hold that exemption is not lost as long as profits are retained by the organization or are used to further the purposes which are made the basis for the exemption, and are *not otherwise* used for the benefit of any private shareholder or individual.

The opinion in this case confuses petitioner's "purposes" with the *means* by which such "purposes" are accomplished, and ignores the settled distinction between *source* and *destination* of income.

4. The question involved is of general importance. The same exempting clause appears in the income tax, estate tax, and gift tax acts.[5]

There is also involved the tax liability of other non-profit hospitals. Over forty-two per cent (2,967 out of 6,991) of all hospitals in this country are "non-profit".[6] They consist of "church, fraternal or other association controlled institutions", and embrace fraternal, railroad, lumbering, steel and many other large employee groups, (Railroad hospitals alone, have well over half million members). All are non-profit, and many are maintained for, and largely supported by, *dues-paying* members. Congress has not distinguished

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[5]I.R.C. Sec. 101(6), 861(a)(3), 1004(a)(2)(B).

[6]"Vital Statistics—Special Reports, Hospital and other Institutional Facilities and Services, 1939", Vol. 13, No. 2, p. 7, issued by Bureau of the Census. Out of 6,991 hospitals, 2,967 (42.44 per cent) are there classed as "nonprofit", 1,729 (24.74 per cent) as "government", and 2,295 (32.82 per cent) as "proprietary".

as between the various kinds of these non-profit hospitals.

5. After the 1937 ruling, petitioner refunded to its employees the taxes theretofore deducted. Thenceforth until 1939, when the ruling was reversed, it discontinued such deductions altogether. Not to have done so would have been a misdemeanor, (Calif. Labor Code, Sec. 216). When the earlier ruling was reversed, it was obliged to pay all earlier *employees'* taxes from its own funds. Moreover, petitioner was required to pay interest on all alleged delinquencies from original due dates, and even heavy penalties for non-payment. This was one of the grounds of the claims for refund, (R. 16).

Denial of relief constituted a palpable abuse of the Commissioner's discretion. It offends common sense, and the moral sense, that, where the *creditor* denies the debt, the taxpayer must pay a heavy additional penalty for not paying that which in no case would have been accepted. Also, in the absence of contract, interest is awarded as damages for *wrongful* detention. A correct determination of this is important to the orderly administration of the revenue laws.

WHEREFORE, petitioner prays that a writ of certiorari issue out of and under the seal of this Honorable Court directed to the United States Circuit Court of Appeals for the Ninth Circuit, commanding that Court to certify and send to this Court, for its review and determination, on a day certain to be therein named, a full and complete transcript of the record

and of all proceedings in said case numbered on its docket 11,029, that the judgment of said Circuit Court be reversed, and that petitioner have such other and further relief in the premises as to this Court may seem proper.

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